

Your VESTED



INTEREST

North Dakota State Investment Board

March 2001

AND IF YOU GO CHASING RABBITS THE 1999-2000 STORY

Welcome to 2001! The fact that you are even reading this proves one thing...you survived the year 2000! And how intact are we feeling having weathered some pretty horrific storms in the investment world? Just when we were getting used to double digit returns on the positive side each and every year! Now this? Beam me up Scotty, this is just too real!

1% in 1998. Graph those three years and you've got one funky bell curve. Is there any lesson here yet? Let's move on...

8 BASIC ASSET CLASSES

Asset Class	Benchmark
Large Cap U.S. Stocks	S&P 500 Index
Large Cap Growth Stocks	S&P 500/BARRA Growth Index
Large Cap Value Stocks	S&P 500/BARRA Value Index
Small Cap U.S. Stocks	Russell 2000 Index
Small Cap Growth Stocks	Russell 2000 Growth Index
Small Cap Value Stocks	Russell 2000 Value Index
International Stocks	MSCI EAFE Index
Domestic Bonds	LB Aggregate Index



NORTH DAKOTA RETIREMENT AND INVESTMENT OFFICE

*Teachers' Fund for Retirement
State Investment Board*

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Other forms of this newsletter are available on request.*

Before we take a look forward to try to make some sense of it all, let's make a few observations about the first year of the new millennium (tired of that word yet?!). Let's segment the investment world into eight basic asset classes and use the most appropriate benchmark to measure the performance of each one (see box). Now that we have defined the investment world by these eight groupings, let's see wasssuupppp???

In 1999, the big winner was the Russell 2000 Growth Index, up 43%! Well, guess who was in last place for the year 2000? Yup, you guessed it, the Russell 2000 Growth Index, down more than 22%, the worst of all the eight asset classes! That's a wild ride, ya think? In case you're not queasy yet, picture this...this same index returned a whopping

Returning to 1999 – the silver medal winner for performance was the S&P 500/BARRA Growth Index, turning in a healthy 28%. So somehow the world changed completely in 2000 and this same index made the perfectly symmetrical nosedive to second-to-last-place, yielding a return of minus 22%. Interestingly enough, this asset class returned 42% in 1998, helping the 3-year investor weather the change in tides.

*When logic and proportion
Have fallen sloppy dead*

Now, the third-place winner in 1999, at +27%, was the MSCI EAFE Index, the benchmark for International Stocks. Have you been paying attention? Okay then, where did this one finish in 2000? If you said third from last, Pavlov's dogs have nothing on you! True, true, our pal

continued inside



*Steve Cochrane, CFA
Executive Director/CIO*

“...AND A TIME TO SOW”

Well, gang, it looks as though the harvest is over, at least for the time being. Four of the last five years have been wonderful for our pension funds from an investment performance perspective. And now it's time for a little payback.

As you know, investment returns by their very nature are volatile. The ride from point A to point B is not a smooth one. And calendar year 2000 is a bump in the road of long-term investment success. At this point, you have read six sentences and have already covered one of the most fundamental foundations of investment finance. Did it get by you? Maybe not, but here it is...volatility is risk.

Okay, we didn't feel the earth shake or anything, but this point is essential in understanding the nature of returns and explaining why investors make the choices they make. Do you remember the TV character, Father Sarducci? He had a way of simplifying matters to their essential root. Economics?

FROM THE DIRECTOR'S CHAIR

Supply and demand. Investments?
Risk and return.

And how do we measure risk? Volatility. Think of it this way... if you invest \$1,000 in a savings account, you can count on getting a regular interest payment. Your account balance always grows by the amount of the interest and there is virtually no risk that you will lose your investment. So you have safety and comfort knowing exactly how much interest you will get and when you will receive it. If you plotted a graph of your account, it would have a straight, slightly upward-sloping line representing the growth of your assets over time. No volatility here, just smooth and steady growth. And how much does all this comfort cost? Well, you have to live with the return, which at today's savings account rates is about 1.01%. No volatility, low risk, low return.

Now let's contrast this with a more volatile situation. Say you decide to take your \$1,000 and buy into some beaten-up tech stock right about now. So you pick one because you believe in the business model and the long-term prospects of the company. Plus, the stock is already down 65% from its previous high point. So in you dive and the next thing you know, some other tech company reports disappointing earnings and your stock pays the price, down 15% after only a week. Yikes! And then the collective wisdom of the market analysts decide that the economy has a 60% chance of going into recession and your stock takes another dive. You have now lost 40% of what you paid for it. Your account is now worth \$600 after 6 months.

Introspection time, folks. Why did I buy this stock in the first place? Now, we won't go through the laundry list of things to review, but

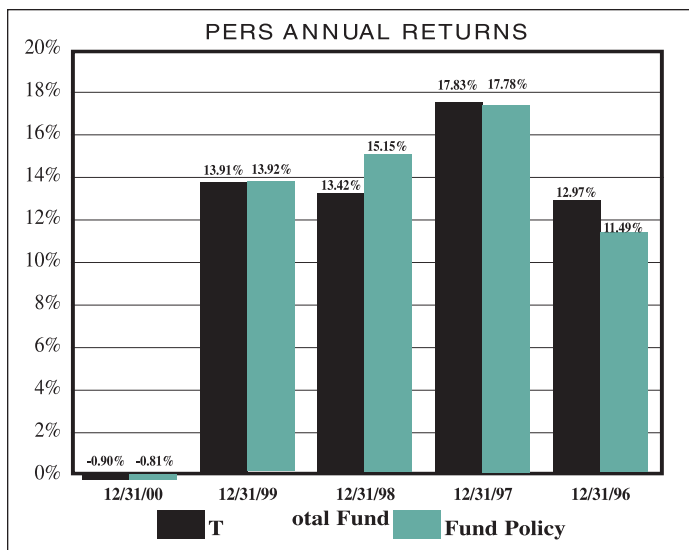
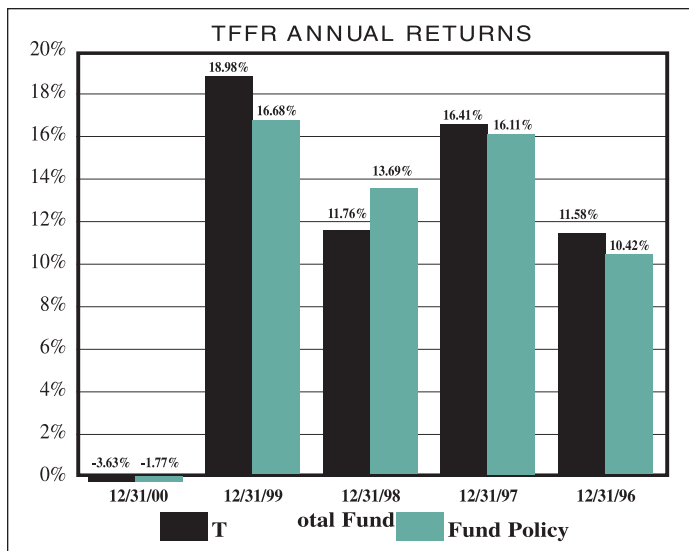
let's just say that after some in-depth research you conclude that you are going to stick it out. Hang on!

The remainder of this example is just for illustrative purposes and should not be construed as rendering investment advice!

Let's say \$600 turns out to be the low point for the year. Yeah! In fact, over the next six months, this stock is up 68.35%! Nice cocktail party conversation. And as the year closes out, this account is worth \$1,010.10 (same as the savings account). What a wild ride! You compare your account with that of your friend who put her money in the savings account and notice that you both had the same return for the year...1.01%! High volatility, high risk, low return. Something wrong here? Well, simply put, high risk does not mean guaranteed high return. But if an investor seeks the opportunity for high return, then they must be willing to take on high risk.

So we can now see how risky situations are characterized by volatility. In order to define risk levels, we need to be able to measure volatility. And we do that with a handy, dandy mathematical tool called standard deviation.

Getting back to our funds though, keep in mind that we will have highs and we will have lows and the average return will be somewhere in between. We use many risk control techniques and are careful to invest prudently for the long run. And in the long run, I am looking forward to a comfortable retirement funded by our retirement plan!



ASSET ALLOCATION AS OF DECEMBER 31, 2000

TFFR

Cash Equivalents 1.6%
Private Equity 4.3%
Emerging Markets Equity 4.4%
International Fixed Income 5.4%
High Yield Fixed Income 6.9%
Domestic Fixed Income 7.7%
Real Estate 10%
Domestic Small Cap Equity 10.8%
International Equity 19.3%
Domestic Large Cap Equity 29.6%

PERS

Cash Equivalents 1.0%
Private Equity 3.0%
Emerging Markets Equity 4.0%
High Yield Fixed Income 4.9%
Real Estate 5.3%
International Fixed Income 5.4%
International Equity 7.7%
Domestic Small Cap Equity 8.2%
Domestic Large Cap Equity 29.5%
Domestic Fixed Income 31.0%

1998	1999	2000
S&P/BARRA 500 Growth 42.16%	Russell 2000 Growth 43.09%	Russell 2000 Value 22.83%
S&P 500 Index 28.58%	S&P/BARRA 500 Growth 28.25%	LB Agg 11.63%
MSCI EAFE 20.00%	MSCI EAFE 26.96%	S&P/BARRA 500 Value 6.08%
S&P/BARRA 500 Value 14.69%	Russell 2000 21.26%	Russell 2000 -3.02%
LB Agg 8.70%	S&P 500 Index 21.04%	S&P 500 Index -9.10%
Russell 2000 Growth 1.23%	S&P/BARRA 500 Value 12.72%	MSCI EAFE -14.17%
Russell 2000 -2.55%	LB Agg -0.82%	S&P/BARRA 500 Growth -22.07%
Russell 2000 Value -6.46%	Russell 2000 Value -1.48%	Russell 2000 Growth -22.43%

CONTINUED FROM COVER, **THE 1999-2000 STORY**

MSCI EAFE wound up third from the bottom with a negative 14% performance.

And the White Knight is talking backwards

And the Red Queen's "off with her head!"

Who came in on top for the year 2000? The gold goes to the Russell 2000 Value, the same index that finished 1999 in, uh huh, last place! Second position for 2000 went to LB Aggregate Index, allowing boring old bonds a well-earned place on the podium. The bonds especially appreciated this as they finished, right again, second from the bottom in 1999.

*When the men on the chessboard
Get up and tell you where
to go*

Just to keep us on our toes, it turns out that the fourth and fifth place finishers were exactly the same in '99 and '00, with Russell 2000 Index edging out S&P 500 Index in both cases. How weird is that?

Go ask Alice! I think she'll know.

WELCOME NEW SIB MEMBERS



Jack Dalrymple
Lieutenant Governor



Jim Poolman
Insurance Commissioner

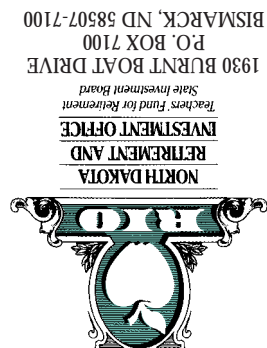
The Lieutenant Governor and the Insurance Commissioner serve as ex officio members of the State Investment Board. Their current term in office expires in December, 2004.

INVESTMENT MANAGER PROFILE CAPITAL GUARDIAN TRUST COMPANY

The North Dakota State Investment Board (NDSIB) employs 20 independent investment management firms. Capital Guardian is one of the managers and is responsible for investments in international and emerging growth market stocks. Below is a brief profile of the firm; additional information can be accessed on our website at www.discovernd.com/rio.

CAPITAL GUARDIAN TRUST COMPANY

Location:	Los Angeles, CA
Assets Under Management:	\$98.4 Billion
Investment Professionals:	23
Representative Clients:	ALCOA, Inc., Dow Corning Corp.
NDSIB Manager Since:	March 1992
Assets Managed for NDSIB:	\$349.2 Million



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